



California Public Employees' Retirement System (CalPERS) Alternative Investment Management Portfolio

Quarterly Report Executive Summary

(as of March 31, 2011)

Presentation Date: June 13, 2011

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1.0 Executive Summary

Private equity is a long-term asset class with performance results influenced by various factors. This report concentrates on several key exposures that contribute to performance results, including sector, geography and vintage year. In addition, broad industry trends are highlighted that may affect performance results going forward.

1.1 Overall Alternative Investment Management (AIM) Program Performance

AIM outperformed the Long-Term Policy Index by 1.8 % but underperformed the Policy Index by 1.4% over the latest ten-year period as of March 31, 2011. AIM also underperformed the Policy Index over the latest three-year and five-year periods. The inclusion of the Custom Young Fund Index¹ in the Policy Index until July 2009 and strong public markets performance post-July 2009 contributed to the Program's underperformance over the longer three-year and five-year periods. Over the latest one-year period, AIM outperformed the Policy Index by 2.3%, reflecting strong results across multiple sectors during the period led by the Buyout and Current Income sectors. The AIM Program has outperformed the Wilshire 2500 ex-tobacco + 300 bps over all periods evaluated.

Performance vs. Policy Benchmarks				
	1 Year	3 Year	5 Year	10 Year
AIM Program²	22.7%	2.4%	10.3%	6.9%
<i>AIM Policy Index³</i>	20.4%	12.5%	14.3%	8.3%
<i>Wilshire 2500 ex-tobacco + 300 bps</i>	20.4%	0.8%	5.9%	5.2%
<i>Long-Term Policy Index⁴</i>	---	---	---	5.1%
Excess Returns				
<i>v. Policy Index</i>	2.3%	(10.1%)	(4.0%)	(1.4%)
<i>v. Wilshire 2500 ex-tobacco + 300 bps</i>	2.3%	1.6%	4.4%	1.7%
<i>v. Long-Term Policy Index</i>	---	---	---	1.8%

¹ The Custom Young Fund Index is composed of private equity holdings that lagged in being written-down as the public markets declined in the reporting period.

² The net asset value of CalPERS' AIM portfolio is lagged one quarter with adjustments for current cash flows through the reporting period

³ Wilshire 2500 ex-tob +3% (from and since July 2009); previous periods for the AIM Policy Index are linked historically to the Custom Young Fund, AIM's prior benchmark

⁴ 10-year Wilshire 2500+3%

1.2 Highlights of Program Activity

- AIM's net cash flow was **positive** (distributions exceeded contributions) for the past two quarters.
- The Buyout sector continues to be the largest proportion of the AIM Program at 63% and was the largest contributor to performance due to continued valuation increases (across all transaction sizes).
- The United States, representing the largest exposure of the portfolio, had the largest impact on performance results over the past year. AIM invests globally and has approximately 39% of NAV is outside of the United States.
- An analysis of the existing unfunded commitments shows that general partners have **substantial “dry powder”** (\$16.0 billion), the majority of which is expected to be deployed within the next three years (as determined by the termination of the investment period).
- Although the Program is in its twenty-first year, the preponderance of value and performance results are being **driven by investments made in the last ten years**.
- The five largest relationships represent approximately 35% of total exposure (defined as market value plus unfunded commitments). Amongst these five firms, capital is allocated across 82 investments (partnerships and direct investments) and targets multiple sectors and geographies. Apollo Management, AIM's largest relationship by total exposure, listed on the New York Stock Exchange on March 30, 2011.

1.3 Industry Trends

- Private equity fundraising activity continued to decline through 2010 but is **on pace for a slightly stronger 2011** calendar year through the first three months of the year. The market may become bifurcated, resulting in the most attractive funds being quickly over-subscribed, with the remainder continuing to struggle in this challenging environment.
- **LBO activity declined** in the first three months of 2011 from the burst of activity in Q4 2010, which many believe was influenced by the potential expiration of tax cuts (that were actually extended).
- **Higher levels of risk appear to be returning to the leveraged buyout market.** Purchase price multiples declined in the first quarter of 2011, but debt multiples continued to increase, resulting in less equity required to complete transactions. Loan volume for dividend recaps continued to be prevalent and actually represents a larger proportion of total lending volume than in the peak years of 2006/2007. In addition, “covenant-lite” loans (few to no restrictive covenants placed on the borrower) have returned to the marketplace.
- **Exit activity for venture capital investments continues to show signs of activity**, across both M&A transactions and IPO market, but has yet to exhibit increases on a consistent basis. Many industry participants believe that there is significant imbedded value within existing venture portfolios, and registration for initial public offerings (IPOs) have increased, but material exits are going to be necessary to positively impact the poor venture returns over the last decade.
- Some of the **larger buyout transactions completed over the last peak cycle are accessing the public markets** through IPOs. IPOs completed year-to-date include HCA (\$3.8 billion raised), Kinder Morgan (\$2.9 billion raised), Nielsen (\$1.6 billion raised) and Freescale Semiconductor (\$0.8 billion raised), which have been generally well received in the marketplace. Dunkin’ Brands and Toys ‘R’ Us are also expected to go public in the near-term.
- The **outlook for distressed debt investment strategies is mixed.** The rebound in debt pricing has minimized the opportunity for trading strategies, and an improved economic environment and the return of more lenient lending reduces the opportunity set for debt-for-control transactions (particularly at the larger end).

1.4 Terms and Conditions

As mentioned in prior reports, the Institutional Limited Partners Association (ILPA) has published the ILPA Private Equity Principles (Principles), a best practice document that was expected to help guide private equity terms and conditions and move the industry a step closer to establishing a set of guidelines that could improve the alignment of interests, enhance fund governance, and provide greater transparency to investors. ILPA released an updated version in January 2011 that is intended to provide increased focus, clarity and practicality. In addition, ILPA released the first of five recommended standardized reporting templates (capital call and distribution notice templates) in an effort to improve uniformity and transparency.

1.5 Additional AIM Program Updates

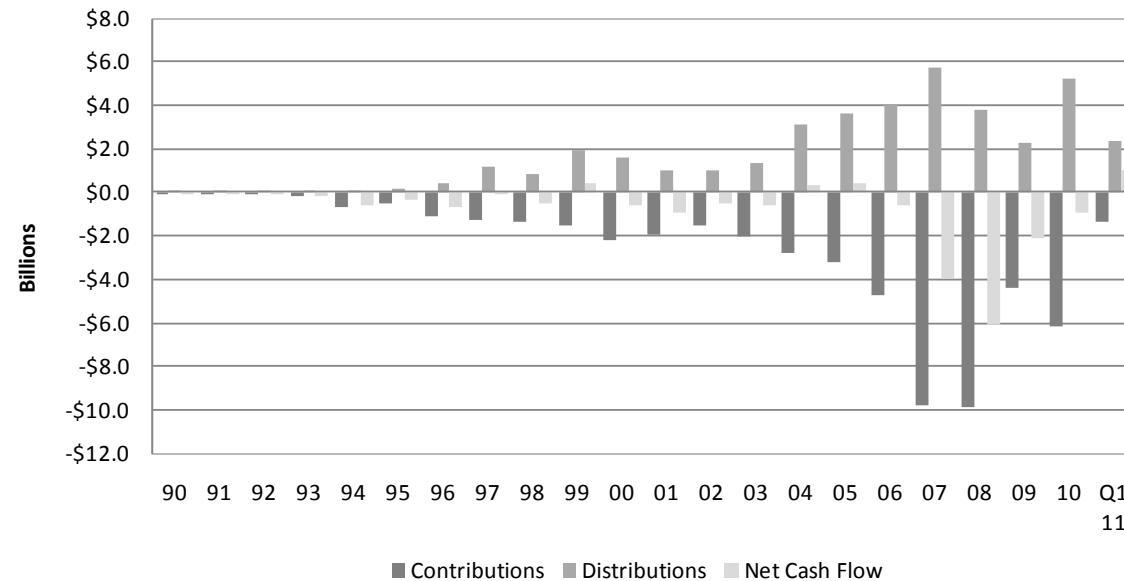
AIM has positions for eighteen private equity professionals. There were **three vacancies** resulting from the departure of its Senior Investment Officer and two Senior Portfolio Managers. In the interim, AIM program staff reported directly to the Chief Investment Officer. On May 31, 2011, Mr. Réal Desrochers was named as the new Senior Investment Officer for AIM.

2.0 AIM Performance Overview

2.1 Portfolio Cash Flows

During the first quarter of 2011, **AIM's net cash flow was positive** (distributions exceeded contributions). Distributions have improved in recent periods, and are expected to continue particularly with a more friendly credit market, the re-emergence of the dividend recap, and a greater use of the IPO market for possible liquidity.

AIM Program Annual Cash Flows

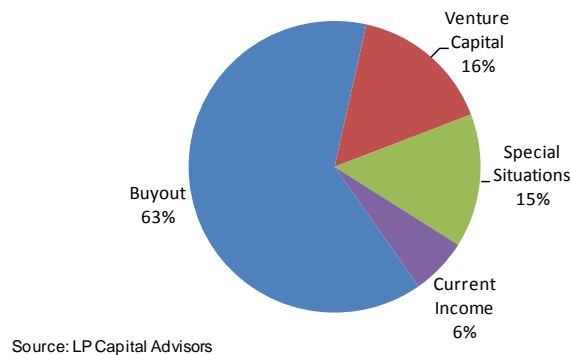


Source: LP Capital Advisors, PCA

2.2 Portfolio Sector Composition and Performance

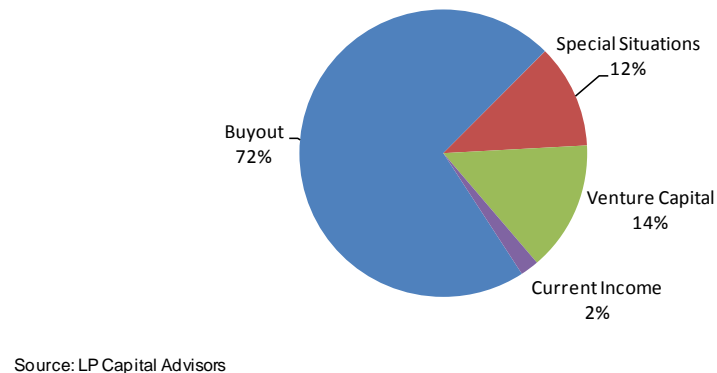
Sector distribution reflects the markets that AIM believes will enable it to produce the expected return imbedded in the Investment Committee's asset allocation decisions. The following charts portray distribution by net asset value (NAV). The **Buyout sector continues to be the largest proportion** of the AIM Program at 63%. Given the material allocation and impact on performance results, this is the first report where Current Income has been presented as a separate sector (previously included in Special Situations).

AIM Program NAV by Sector: \$32.6 B

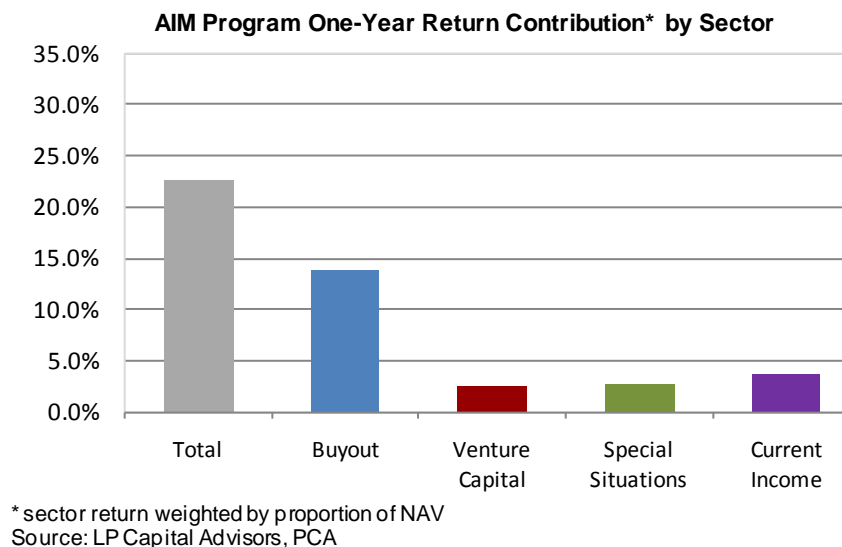


Sector-wise, Buyouts represent the greatest proportion of the Program's unfunded commitments and will therefore continue to be the largest exposure within the AIM Program going forward.

AIM Program Unfunded Commitments by Sector: \$16.0 B



While all major sectors of the AIM Program contributed positive results over the latest year, **Buyouts were the largest contributor** to performance as the material exposure to the sector continued to experience valuation increases (across all transaction sizes). Despite representing only 6% of the AIM Program, the Current Income sector was the second largest contributor to results over the latest year with the rebound in debt prices.

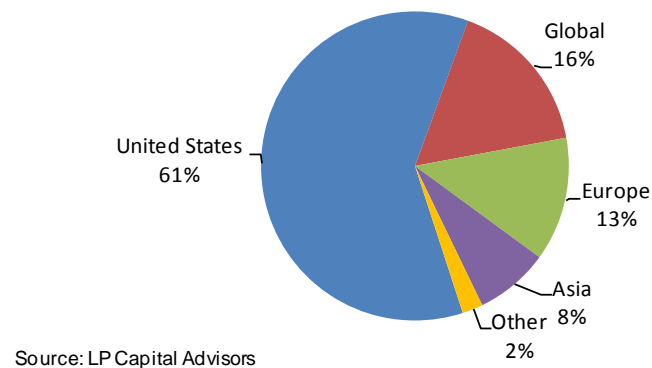


Over the latest three-year period, the AIM Program posted a 2.4% average annual return. The Buyout sector (with a 0.9% return) was the largest factor in results over the latest three-year period due to its large allocation. The three-year results reflect the difficult investment environment and associated valuation declines during the economic crisis. In addition, implementation of ASC 820 (previously FAS 157) contributed to the volatility of valuations over this time period as assets were “marked-to-market.” The Buyout sector has generated attractive results over the longer five-year and ten-year periods, posting average annual returns of 11.8% and 12.0%, respectively.

2.3 Portfolio Geographic Composition and Performance

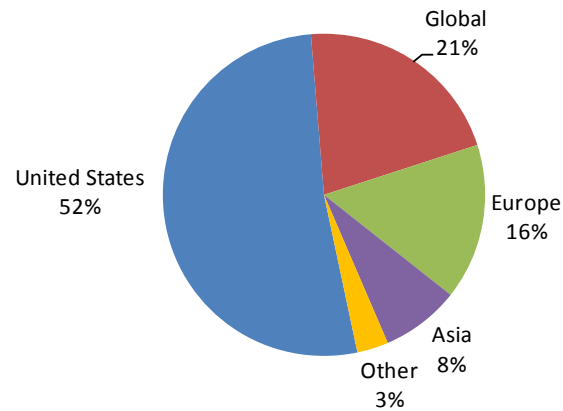
AIM, like CalPERS' other asset classes, invests globally. Approximately **39% of AIM's NAV is outside of the United States**, highlighting the global nature of the Program.

AIM Program NAV by Geography: \$32.6B



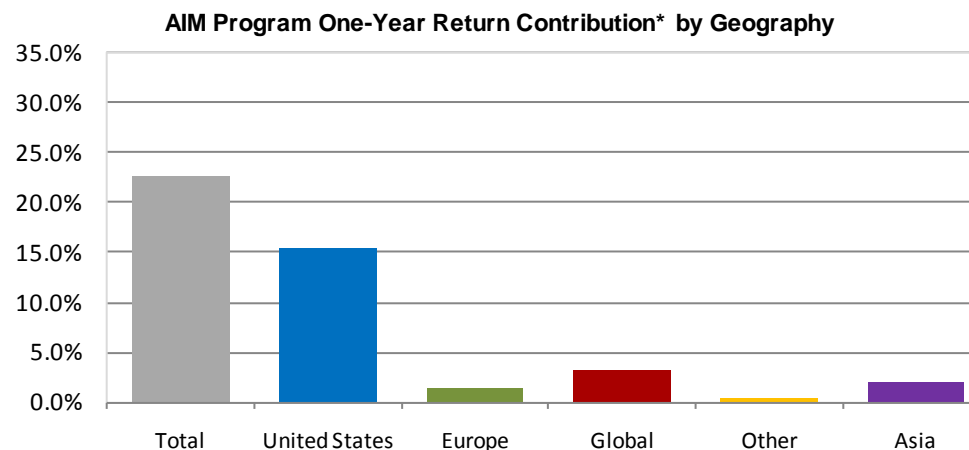
During the quarter, AIM's geographic allocation was impacted by significant shifts by Global funds to the United States, as based on partnership strategy categorization. However, over the longer term, the United States is expected to receive only 52% of remaining unfunded commitments, thereby increasing the global nature of the AIM Program going forward.

AIM Program Unfunded Commitments by Geography: \$16.0 B



Source: LP Capital Advisors

Performance results remained in positive territory across all geographic sectors over the latest one-year period. The **United States, representing the largest exposure of the portfolio, had the largest impact on performance** results over the past year. AIM's Global exposures provided the second largest positive contribution, as many of the large Buyout funds and Special Situation funds that generated strong results over the latest year are categorized as global mandates.



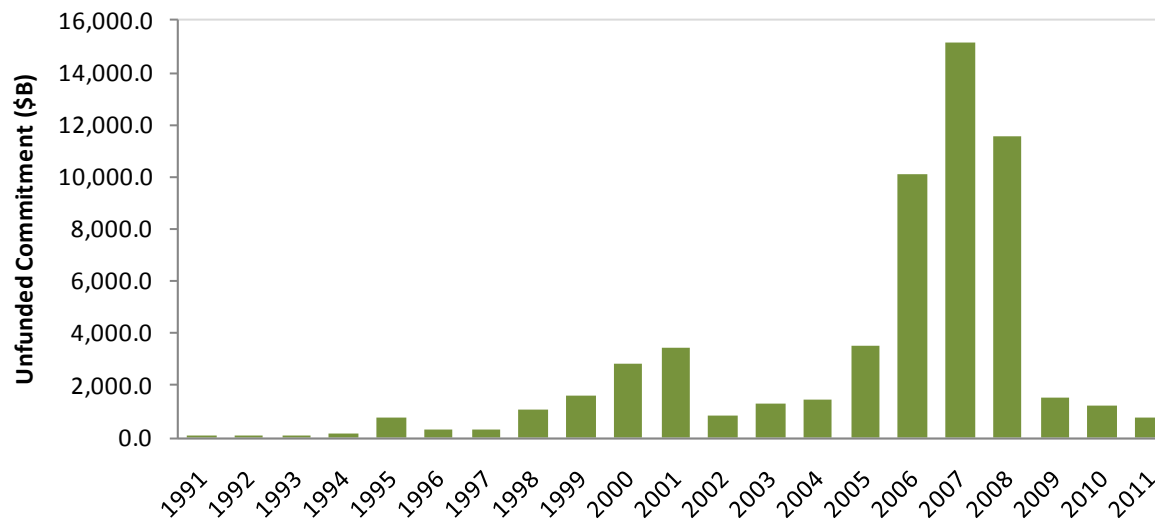
* geographic return weighted by proportion of NAV
Source: LP Capital Advisors, PCA

Over the latest three-year period, AIM's Europe exposure was the largest detractor from performance as the AIM Program posted a 2.4% return. AIM's Europe exposure posted an average annual return of minus (5.3%). The United States offset some of the declines over the latest three-year period with a 2.9% average annual return. The United States has historically represented the largest geographic component of the Program but this has decreased over recent years with the globalization of the portfolio. The United States exposure posted average annual returns of 9.8% and 8.7% over the latest five-year and ten-year periods, respectively. AIM's Europe exposure has contributed to long-term results, generating strong returns of 14.4% and 15.8% respectively, over the longer five-year and ten-year periods.

2.4 Portfolio Vintage Year Composition and Performance

Since the AIM Program began in 1990, it has committed \$66.6 billion in aggregate commitments and currently has \$57.5 billion in active commitments. Consistent with the behavior of other large private equity investors, **AIM made very few new commitments in recent years** (\$1.5 billion during 2009, \$1.2 billion in 2010 and \$750 million at Q1 2011).

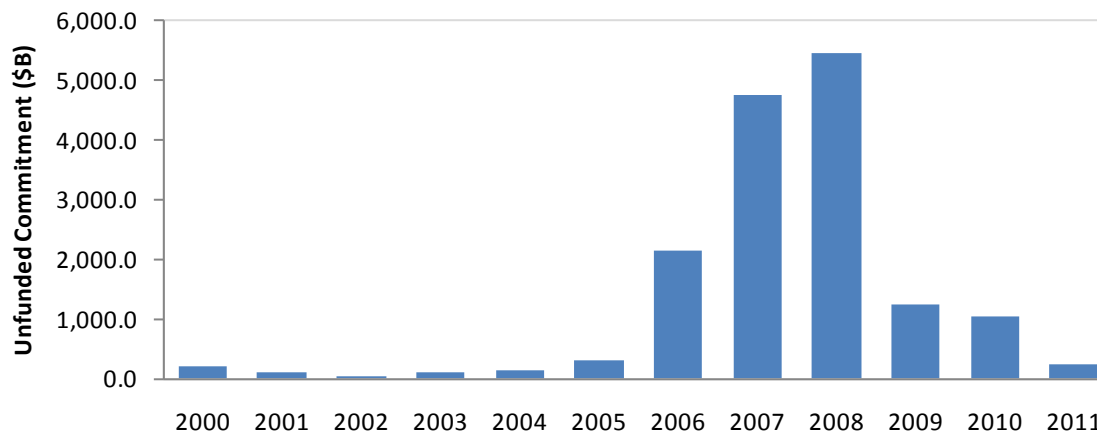
AIM Program Active Commitments by Vintage Year: \$57.5 B



Source: LP Capital Advisors

An analysis of the existing unfunded commitments shows that **general partners have substantial “dry powder”** (\$16.0 billion) to pursue investments consistent with the strategies contained in their limited partnership agreements with AIM. In 2006, \$10.1 billion was committed and remains 21% unfunded as of March 31, 2011. Commitments in 2007 and 2008 were \$15.2 billion (31% unfunded) and \$11.5 billion (47% unfunded), respectively. Only \$1.5 billion of commitments were made in 2009, \$1.2 billion of which remains unfunded (80% unfunded). The 2010 commitments of \$1.2 million have drawn approximately \$125 million in contributions and are 89% unfunded. The 2011 commitments at March 31, 2011 have not yet drawn material capital.

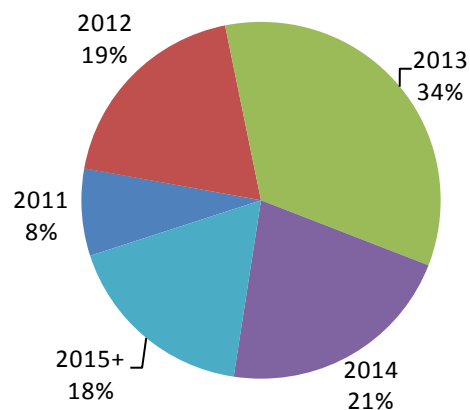
AIM Program Unfunded Commitments by Vintage Year: \$16.0 B



Source: LP Capital Advisors

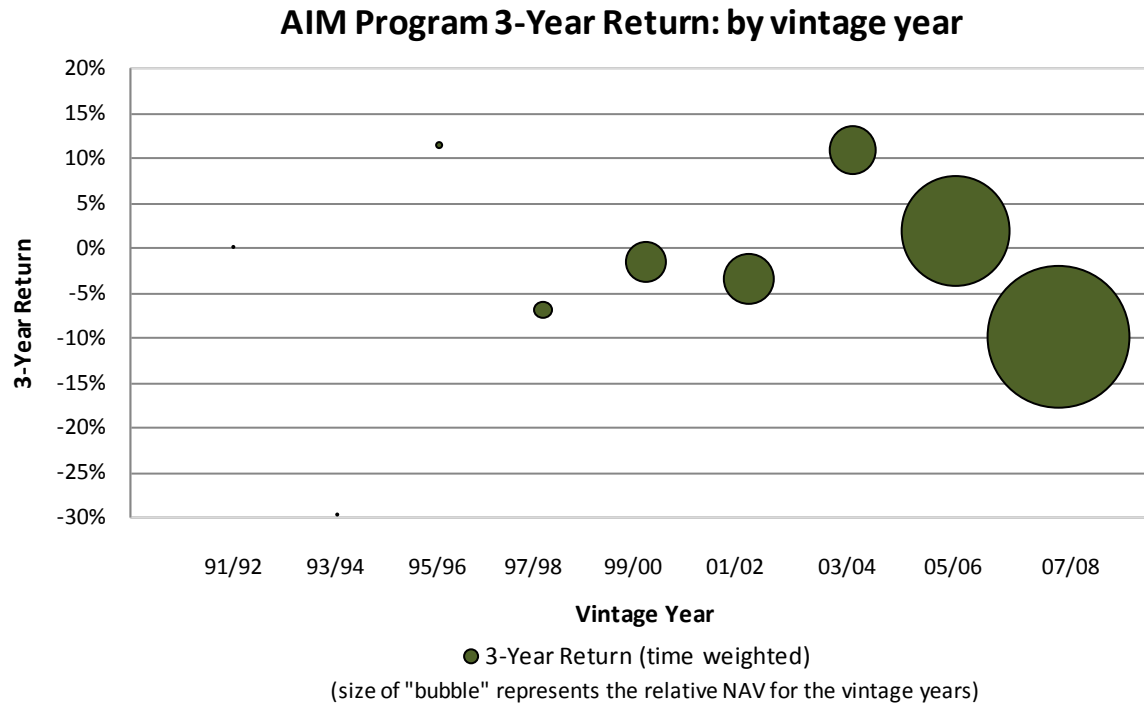
The majority of unfunded commitments are expected to be **deployed within the next three years** (as determined by the termination of the investment period). However, the pace at which capital is drawn down is primarily at the discretion of each general partner and may be called at any time.

AIM Program Unfunded Commitments by Termination of Investment Period



Source: LP Capital Advisors, PCA

The following chart depicts the distribution of returns and net asset values by vintage years for the AIM Program. Although the Program is in its twenty-first year, the preponderance of value (represented by the size of the “bubble”) and **performance results are being driven by investments made in the last ten years.**



Source: LP Capital Advisors, PCA

2.5 Annual Commitment Activity and Manager Concentration

The AIM Program has committed to four opportunities at March 31, 2011 categorized as a 2011 vintage.

AIM Commitment Activity: 2011 Vintage

<u>Partnership</u>	<u>Commitment</u>	<u>Sector</u>	<u>Relationship</u>
GSO Capital Opportunities Fund II, L.P.	\$250 M	Credit Opportunities	Existing
Birch Hill Equity Partners (US) IV, L.P.	\$150 M	Canadian Middle Market	Existing
Oaktree Opportunities Fund VIIIb, L.P.	\$200 M	Distressed	Existing
Avenue Special Situations Fund VI, L.P.	\$150 M	Distressed	Existing

The five largest relationships, based on total exposure (defined as market value plus unfunded commitments) are listed below. Amongst these five firms, capital is allocated across 82 investments (partnerships and direct investments) and targets multiple sectors and geographies. Apollo Management, AIM's largest relationship by total exposure, listed on the New York Stock Exchange on March 30, 2011.

Largest AIM Relationships by Total Exposure

<u>Firm</u>	<u>Investments</u>	<u>Total Exposure (\$M)</u>	<u>% of Program</u>
Apollo Management	14	5,433	11%
Carlyle Group	34	4,947	10%
TPG Capital	16	2,718	6%
Blackstone Group	10	2,087	4%
CVC Capital Partners	8	1,961	4%

Source: LP Capital Advisors, PCA

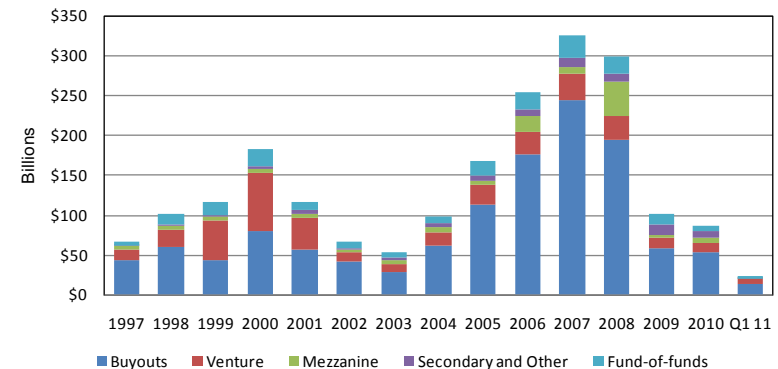
3.0 Private Equity Market Environment

Fund Raising Trends

- Fund raising activity continued to decline through the calendar year of 2010 raising \$86.3 billion in domestic commitments, down 16% from the \$102.2 billion raised in 2009.
- Only \$23.5 billion raised in the first quarter of 2011. Annualizing the activity year-to-date for 2011 suggests \$93.6 billion in commitments for 2011.
- Buyouts continued to lead fund raising activities in the first quarter of 2011 raising \$14.7 billion of commitments, followed by venture capital at \$5.1 billion, fund-of-funds at \$2.7 billion, secondary and "other" at \$0.6 billion, and mezzanine at \$0.4 billion.

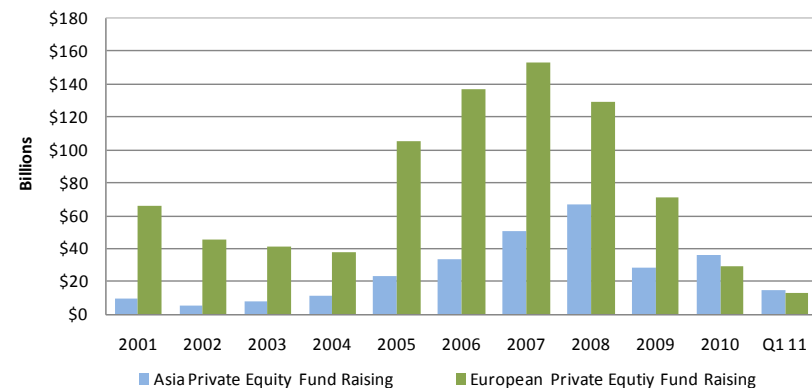
- Commitments to private equity partnerships outside of the U.S. have exhibited similar declines in fund raising activity over the past several years.
- Commitments to European funds had outpaced those to Asian private equity funds over most periods with both regions trailing the activity of the U.S. markets.
- In 2010 and year-to-date, Asia has broken with this trend as commitment levels to Asia have exceeded the capital raised by the European markets, according to Thomson Reuters's data.

Commitments to U.S. Private Equity Partnerships



Source: Private Equity Analyst through March 2011

Commitments to Non-U.S. Private Equity

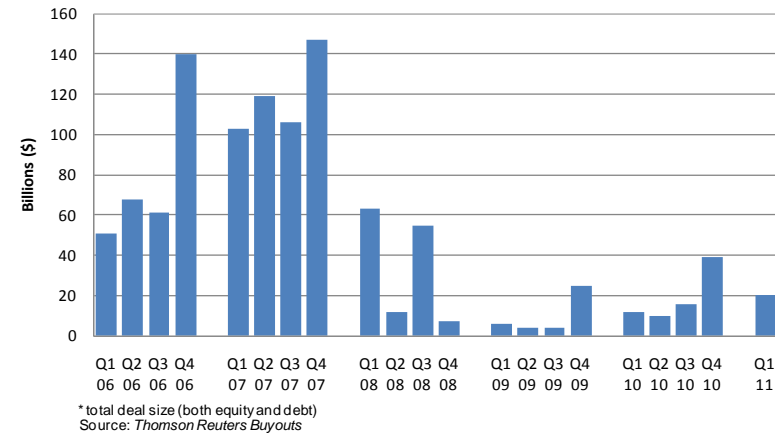


Source: Thomson Reuters

U.S. Buyout Market Trends

- Buyout transaction activity increased in the second half of 2010 as the economy appeared to be stabilizing and access to credit was improving.
- U.S. buyout deal volume decreased to \$20 billion in the first quarter of 2011 after transacting \$39 billion in the fourth quarter of 2010. However, if this transaction pace is maintained over the next three quarters, 2011 activity levels would be the highest since 2008, which transacted \$137 billion.
- In the first three months of 2011, platform investments represented the largest proportion of transactions at 54%. This is a shift from the prior two years as add-on acquisitions represented the largest proportion of transactions in 2010 (at 41%) and approximately 48% of buyout deals in 2009.
- LBO activity remains well below the peak transaction levels of \$320 billion and \$475 billion for 2006 and 2007, respectively.
- Use of the IPO market has increased for some of the larger buyout transactions completed over the last cycle. IPOs completed year-to-date include, HCA (\$3.8 billion raised), Kinder Morgan (\$2.9 billion raised) and Nielsen (\$1.6 billion raised), which have been well received in the marketplace. Dunkin' Brands, Freescale Semiconductor, and Toys 'R' Us are also expected to go public in the near-term.

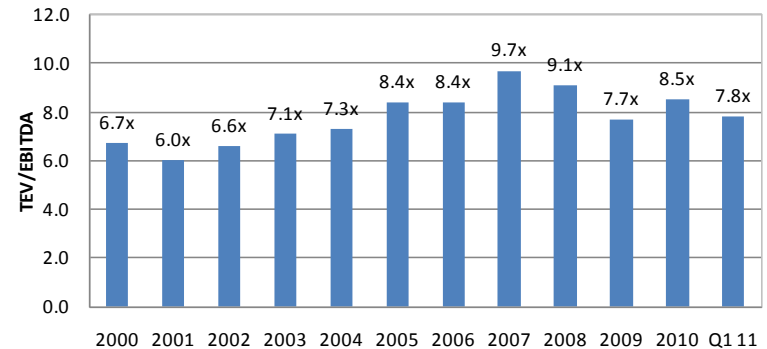
Disclosed U.S. Quarterly LBO Deal Value*



Purchase Price Multiples

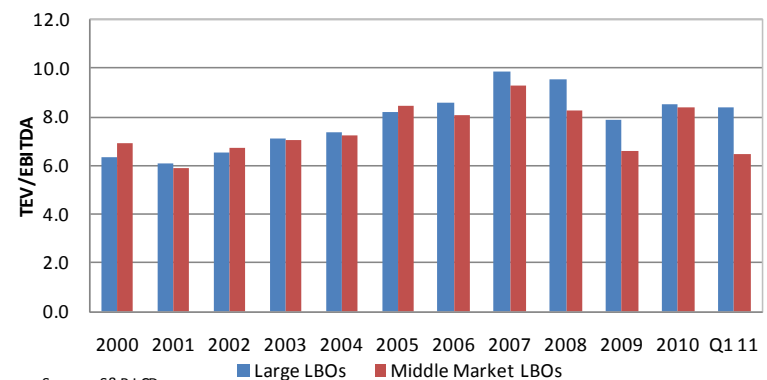
- Purchase price multiples (as represented by total enterprise value divided by earnings before interest, taxes, depreciation and amortization) have exhibited volatility over the past two years. Purchase price multiples initially declined from their 2007 peak to a near-term low in 2009, but rebounded to 8.5x as of year-end 2010.
- As of the end of the first quarter of 2011, the purchase price multiple declined to 7.8x which is in-line with the ten-year average for the industry (7.9x). The initial decline in purchase price multiples can be attributed to valuations under pressure and the lack of available financing. However, many industry participants believe that the increase in purchase price multiples had been impacted by the significant amount of “dry powder” remaining in the industry combined with the approaching investment period termination causing general partners to feel pressured to deploy capital.
- Debt financing for new deals improved throughout 2010, particularly for larger, fast-growing companies, potentially contributing to increased purchase price multiples.
- Purchase price multiples for larger transactions (EBITDAs >\$50 million and represented by the blue bars) have historically been higher than the purchase price multiples exhibited in the smaller and middle market (EBITDAs <\$50 million and represented by the red bars). Given the expected focus on commitments to smaller/middle market opportunities over the near-term, there could be additional competition for deals going forward that could influence the purchase price multiple in the smaller end of the market.

Purchase Price Multiples



Source: S&P LCD

Purchase Price Multiples: large vs middle market

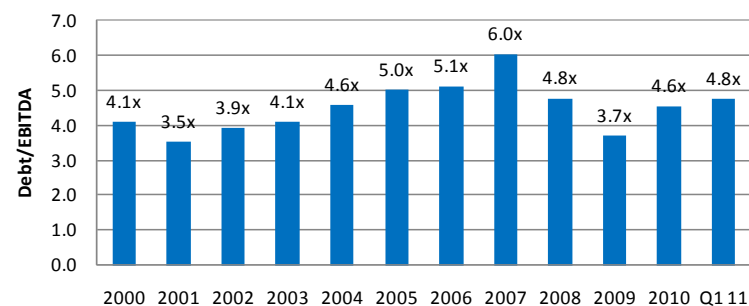


Source: S&P LCD

Debt Multiples

- The average debt multiple also declined from a peak in 2007 to a recent low in 2009 only to rebound in 2010 and the first quarter of 2011.

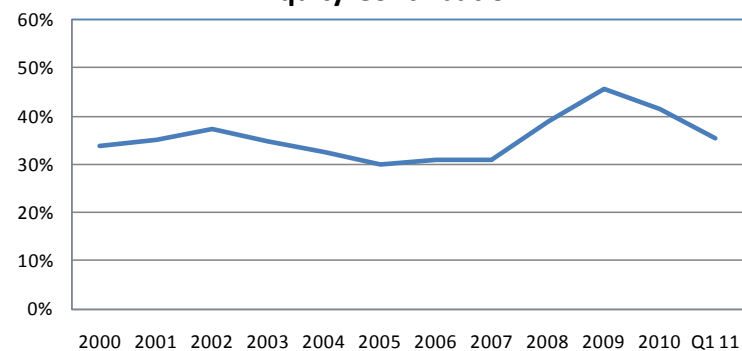
Average Debt Multiples



Source: S&P LCD

- These dynamics had resulted in more conservative capital structures for transactions completed in 2009 and early 2010. However, the equity component of a transaction has already declined to an average of 35% in Q1 2011.

Equity Contribution



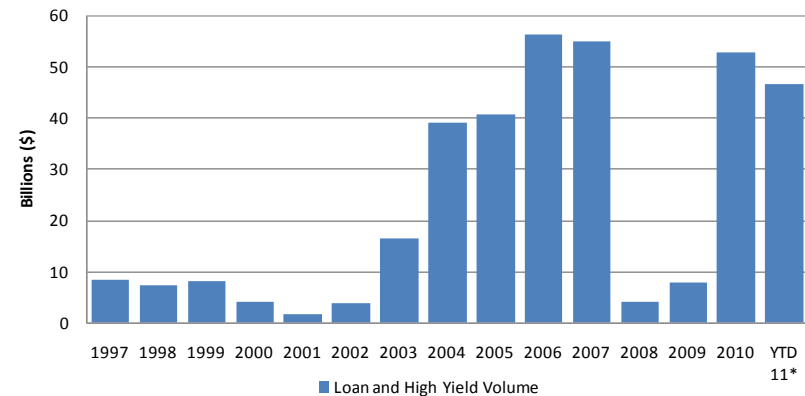
Source: S&P LCD

Dividend Recaps

- The private equity market saw a re-emergence of dividend recaps and stock repurchase activity in 2010, which had virtually disappeared post credit bubble.
- Increasing leverage, and ultimately risk, at the portfolio company level.

- Dividend loan volume is currently a greater proportion of overall activity than in the prior peak in the 2006/2007 time period.

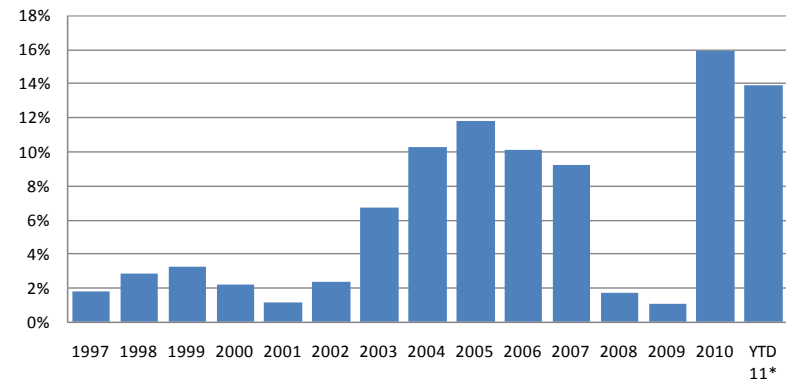
Dividend/Stock Repurchase Loan Volume



* through 5/13/2011

Source: S&P LCD, Bank of America Merrill Lynch

Dividend Loan Volume: as % of Total Loan Volume



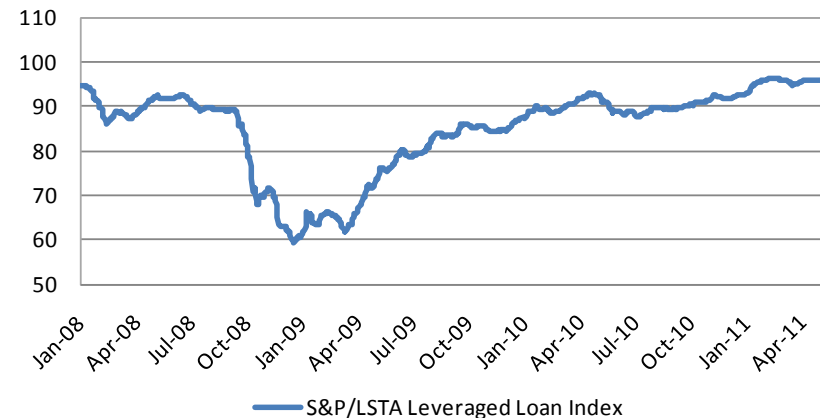
* through 5/13/2011

Source: S&P LCD, Bank of America Merrill Lynch

Distressed Debt

- The outlook for distressed debt investment strategies is mixed. The rebound in debt pricing has minimized the opportunity for trading strategies. As highlighted in the chart below, the renewed interest in the leveraged loan market has pushed the price of leveraged loans back to par and near highs.

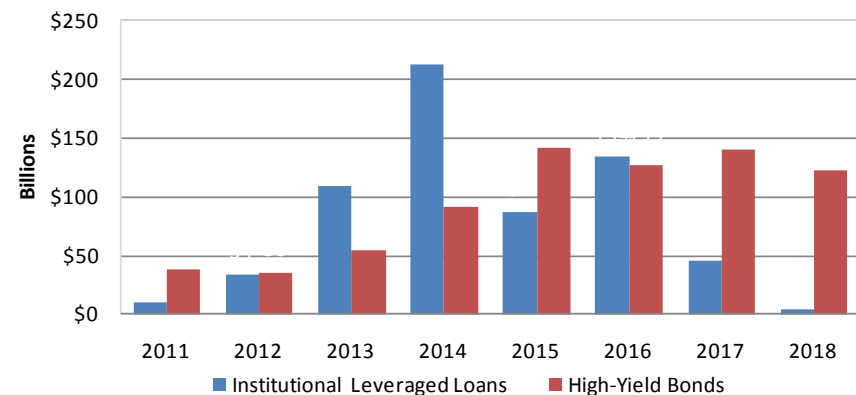
Leveraged Loan Index



Source: Loan Syndications and Trading Association (LSTA)

- The opportunity set for debt-for-control strategies remains unclear. There appears to be an attractive pending opportunity set with the magnitude of debt that was “amended and extended” during the crisis resulting in a significant volume of debt issues that are maturing over the next several years. However, with an improved economic environment and the return of more lenient lending (i.e. covenant lite), the opportunity set for debt-for-control transactions may be less than expected (particularly at the larger end).

U.S High Yield and Leveraged Loan Maturities

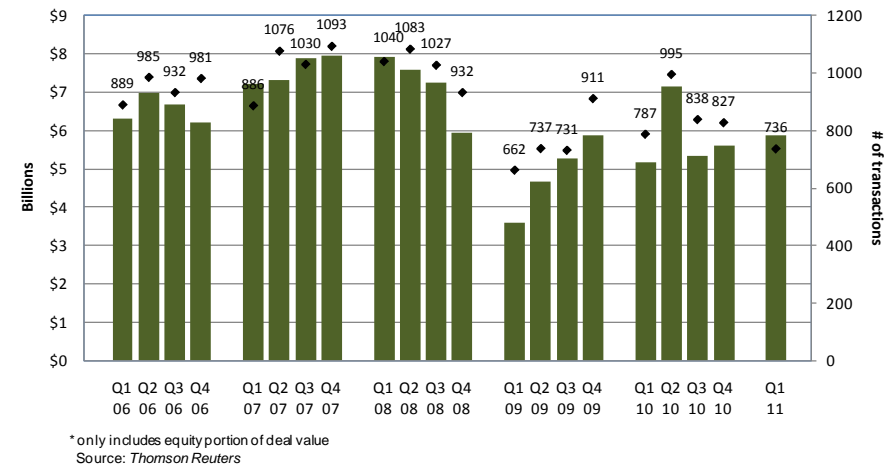


Source: Credit Suisse, Cerberus

U.S. Venture Capital Trends

- Several favorable dynamics in the industry that suggest potential for attractive long-term results going forward, including: reduced commitment to venture capital (i.e. less capital chasing deals resulting in better pricing and less competition), ability for entrepreneurs to create new companies at a lower cost due to ongoing technological enhancements, embedded value within existing venture capital portfolios that have yet to be realized and an improving exit environment.
- Venture capital investment activity increased throughout 2009, 2010, and Q1 2011. In the first quarter of 2011, 736 companies received approximately \$5.9 billion of capital which was just slightly above the quarterly average from last year.
- Approximately \$21.8 billion was invested across 3,277 transactions in 2010, up from \$18.3 billion invested across 2,927 transactions in 2009.
- In comparison, approximately \$28.0 billion was invested across more than 3,900 companies during 2008 and 4,000 companies attracted \$30.5 billion of venture capital investment in 2007.

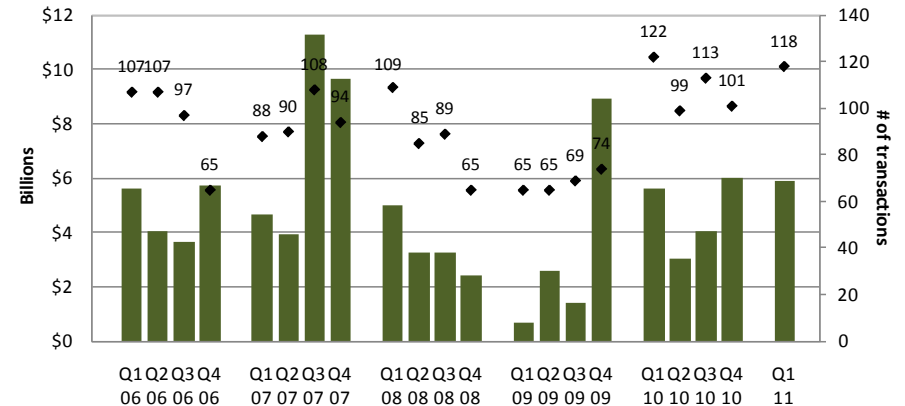
Quarterly U.S. Venture Capital Deal Volume*



Venture Capital Exit Environment

- Exit opportunities for venture-backed companies continue to show signs of increased activity. In 2010, 422 venture-backed M&A transactions representing \$18.4 billion in value were completed, well above the \$13.6 billion in value invested across 273 transactions in 2009. During the first quarter of 2011, \$5.9 billion was completed across 118 transactions

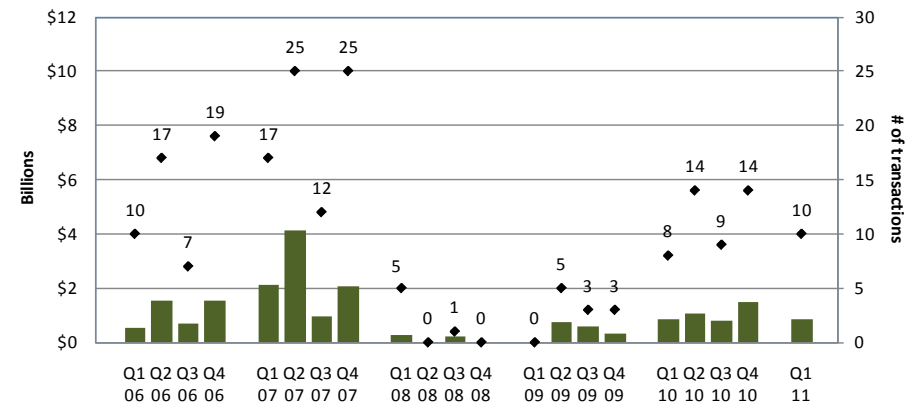
Quarterly U.S. Venture Capital M&A Activity



Source: Thomson Reuters

- IPO activity continues to show signs of life as 10 venture-backed companies went public in the first quarter of 2011 raising \$0.8 billion. Last year, 45 venture-backed companies went public, raising \$4.1 billion while only eleven venture backed companies went public in 2009, raising \$1.6 billion.
- LinkedIn completed a very successful IPO in May of 2011 potentially signaling a surge in IPO activity, particularly for social media companies.

Quarterly U.S. Venture Capital IPO Activity



Source: Thomson Reuters

Appendix 1: AIM Relationships by Total Exposure

<u>Firm</u>	<u>Total Exposure (\$M)</u>	<u>% of Program</u>
Apollo Management	5,433	11%
Carlyle Group	4,947	10%
TPG Capital	2,718	6%
Blackstone Group	2,087	4%
CVC Capital Partners	1,961	4%
Grove Street Advisors	1,659	3%
Silver Lake	1,504	3%
KKR	1,410	3%
Hellman & Friedman	1,126	2%
57 Stars	1,068	2%
Advent International	1,063	2%
Ares Management	1,020	2%
Centinela Capital Partners	885	2%
Yucaipa Companies	875	2%
Avenue Capital Group	855	2%
First Reserve	758	2%
Health Evolution Partners	667	1%
Aurora Capital Group	657	1%
Bridgepoint Capital	648	1%
SL Capital Partners	645	1%
WL Ross & Co	634	1%
Leonard Green & Partners	611	1%
Oak Hill Investment	560	1%
Providence Equity	539	1%
New Mountain Capital	530	1%
Lombard Investments	526	1%
TowerBrook Capital	522	1%
Arclight Capital	476	1%
Hamilton Lane	451	1%
Wayzata	451	1%
KMCP Advisors	428	1%
THL Partners	416	1%
Conversus Asset Management	406	1%
Coller Capital	405	1%
MHR	404	1%
Oak Hill Capital Partners	374	1%
Capital Dynamics	362	1%

<u>Firm (continued)</u>	<u>Total Exposure (\$M)</u>	<u>% of Program</u>
Madison Dearborn	353	1%
Asia Alternatives	343	1%
Welsh Carson Anderson & Stowe	341	1%
Permira	330	1%
Audax Group	287	1%
Francisco Partners	286	1%
Khosla Ventures	273	1%
Birch Hill Equity	258	1%
SAIF Partners	257	1%
Clearwater Capital	239	<1%
Clessidra Capital	234	<1%
Levine Leichtman	214	<1%
Oaktree Capital	201	<1%
KPS Capital Partners	193	<1%
The Jordan Company	188	<1%
Lion Capital	187	<1%
Huntsman Gay Capital Partners	182	<1%
Enterprise Investors	179	<1%
Palladium Equity Partners	178	<1%
W Capital	177	<1%
Lime Rock Partners	165	<1%
Aisling Capital	156	<1%
Affinity Equity	152	<1%
Wellspring	150	<1%
Court Square	147	<1%
Riverwood	137	<1%
Magnum Capital	128	<1%
TA Associates	124	<1%
VantagePoint Venture Partners	117	<1%
Essex Woodlands Health	114	<1%
Clarus Ventures	112	<1%
Insight Capital	109	<1%
ACON Investments	102	<1%
Crimson Capital	102	<1%
Tricor	101	<1%
Quadrangle	101	<1%
GGV Capital	100	<1%
Other (30 partnerships)	1,847	4%